investor's eye

Index

Take Five

Scrip	Reco Date	Reco Price	CMP	Target
Balaji Tele	9-July-07	231	**247**	303
HUL	24-Nov-05	172	**196**	280
HCL Tech	30-Dec-03	103	**324**	395
Madras Cement	17-Nov-05	1,498	**3,300**	3,700
SBI	19-Dec-03	476	**1,607**	1,780

Pulse Track

Large-caps vulnerable to a downturn in the markets

In this update we have tried to identify the stocks that are more vulnerable to a correction in the event of a "U" turn in the foreign fund inflows, which touched a record high of $5.8 billion in July 2007. In order to identify such stocks we have applied three filters (or conditions) on the Nifty stocks and our results are stated in the table below.

Conditions

A. Last three months' absolute price change is positive.

B. Total foreign institutional holding is at least 15% as on June 2007.

C. There has been an increase in the foreign institutional holding during the last nine-month period (September 2006 to June 2007).

Methodology

If the condition is satisfied it is denoted by "1" or else "0" is displayed.

The "COUNT" column shows the addition of the three conditions A, B and C. If "3" is displayed it indicates all three conditions are satisfied, "2" denotes any two of the three conditions are satisfied and so on.

Observation

Reliance Energy, Tata Steel, Grasim Industries, Larsen & Toubro, Bharat Heavy Electricals, ABB and HDFC are more vulnerable to a sharper correction than the other large-caps with an average three-month return of over 32%. State Bank of India and Reliance Petroleum, though satisfy only one condition, still remain highly vulnerable to a correction due to the sharp appreciation in their stock prices in the last three months.

Stocks with a high dividend yield

We have also compiled a list of high dividend yielding stocks, which are generally fancied by investors in times of high volatility and uncertainty in the market.

Conclusion

We have been advising caution in the market for quite some time now but the continuous flow of negative news related to the US subprime saga and its negative impact on global hedge funds and banks are not a good sign for the global equity markets. Hence if the markets witness a sharp correction, then the stocks with "High" vulnerability are more likely to undergo a sharper correction compared with the other stocks in the short term. The views expressed in this article could be contrary to what we have expressed in our fundamental research reports. Hence, we would like to reiterate that this view holds only in the short term and doesn't influence our long-term view on the markets and on specific stocks under our coverage which remains positive.

Stocks vulnerable to FII flow reversal

Large-cap companies	Price chg (%)	% FII holding #	*	Conditions A	B	C	Count	Vulnerability
Reliance Energy	50	21	1	1	1	1	3	High
Tata Steel	18	22	1	1	1	1	3	High
Grasim Ind	17	23	2	1	1	1	3	High
L&T	44	17	0	1	1	0	2	High
BHEL	40	19	-3	1	1	0	2	High
ABB	34	17	0	1	1	0	2	High
HDFC	26	78	-1	1	1	0	2	High
SBI	53	11	0	1	0	0	1	High
RPL	42	3	0	1	0	0	1	High
HDFC Bank	17	26	-7	1	1	0	2	Medium
Tata Power	16	16	-4	1	1	0	2	Medium
Reliance Comm	16	12	1	1	0	1	2	Medium
Reliance Ind	16	20	0	1	1	0	2	Medium
ACC	13	16	-7	1	1	0	2	Medium
SAIL	11	6	2	1	0	1	2	Medium
Zee Ent	10	30	-3	1	1	0	2	Medium
IPCL	15	11	-4	1	0	0	1	Medium
Sterlite Ind	12	6	0	1	0	0	1	Medium

As on June 2007 Source: Sharekhan Research
* Change over last three quarters

High dividend yield stocks

Company	Dividend yield (%)
Ashok Leyland	4.1
Balrampur Chini	3.7
Hind Unilever	3.0
Godrej Consumer	2.7
Ambuja Cement	2.6
HCL Technologies	2.6
Hero Honda Motor	2.5
Ranbaxy Lab	2.3
ITC	1.9
Dabur India	1.7

The author doesn't hold any investment in any of the companies mentioned in the article.

Pulse Track

IIP below market estimates in June 2007

The Index of Industrial Production (IIP) grew by 9.8% year on year (yoy) in June 2007 compared with the market estimate of an 11% growth. The manufacturing sector has shown moderation in growth month on month while electricity production continues to improve yoy. For FY2008 the year to date (YTD) growth in all the three sectors remained at par or was slightly better than that in June 2006.

Manufacturing growth at 10.6%

The manufacturing sector grew by 10.6%, however the growth rate has slowed down on a month-on-month basis from 11.1% in May 2007. Notably, growth in the food segment--with the third highest weightage of 9.1% in the manufacturing sector—slowed down to 1.3% in June 2007 from 24.8% in May 2007. The slowdown was on top of a decline of 3.7% reported in June 2006. We have been stating that the high growth in the food and wood sectors is unsustainable and once this wanes off the manufacturing growth will decline.

Growth in capital goods continues to be robust

The Capital Goods Production Index reported a y-o-y growth of 29% over a higher base of 21.6% of last June, which is commendable. The year-to-date FY2008 growth for the capital goods sector stood at 22.3%, slightly higher than 21% registered in FY2007. The order backlog and new order flows continue to remain robust for most capital goods and engineering companies, hence the outlook on growth for this sector remains positive.

Growth in consumer durables lower than 1%, likely due to lower demand for automobiles

The Consumer Goods Production Index grew by only 4.2% in June 2007 compared with a 6.1% y-o-y growth in June 2006. The durables growth was below 1% (mainly due to a slowdown in the demand for automobiles which has led many large players to cut production) while the non-durables growth was up at 5.4%. The growth in non-durables has declined month on month and so has the growth in the food products category. Both these segments are largely influenced by the sugar production trend, hence we expect the growth in sugar production to have moderated on a month-on-month basis.

IIP up 9.8%—manufacturing growth lower at 10.6%

In % yoy chg	June 2007	June 2006	May 2007	YTD FY08	YTD FY07
IIP	9.8	9.7	10.9	11.0	10.5
General					
Manufacturing	10.6	10.7	11.7	11.9	11.7
Mining	3.6	4.7	3.6	3.2	3.6
Electricity	6.8	4.9	9.4	8.3	5.3
Use based					
Capital goods	29.0	21.6	22.9	22.3	21.0
Consumer goods	4.2	6.1	9.9	9.9	8.5
- Durables	0.6	19.9	3.5	3.0	15.0
- Non-durables	5.4	1.8	12.3	12.4	6.3

Growth in manufacturing sector (% y-o-y change)

Manufacturing sector	Weight	Feb-07	Mar-07	Apr-07	May-07	Jun-07
Food products	9.1	11.1	28.4	53.5	24.8	1.3
Beverages, tobacco and related products	2.4	9.4	5.3	6.4	6.5	9.8
Cotton textiles	5.5	11.7	20.7	9.5	6.9	8.1
Wool, silk and man-made fibre textiles	2.3	6.1	14.6	1.2	10.9	5.0
Jute & jute textiles	0.6	-88.0	-37.7	17.8	40.4	35.2
Textile products incl. wearing apparel	2.5	14.6	15.8	12.4	9.9	14.6
Wood and wood products	2.7	128.9	114.1	92.2	132.8	103.9
Paper & paper products	2.7	7.9	5.6	0.6	0.0	2.3
Leather & leather products	1.14	8.5	-10.0	11.9	5.7	7.7
Chemicals & chemical products	14.0	6.7	15.2	8.6	5.9	4.3
Rubber, plastic, petroleum & coal products	5.7	12.8	16.6	14.0	9.4	9.3
Non-metallic mineral products	4.4	9.2	10.2	7.4	6.7	4.0
Basic metal and alloy industries	7.5	27.4	23.5	18.0	21.1	21.1
Metal products	2.8	-2.2	47.7	6.4	8.4	-7.7
Machinery and equipments	9.6	12.7	13.3	16.2	22.8	18.6
Transport equipment	4.0	12.3	13.6	5.0	-0.1	0.8
Other manufacturing industries	2.6	7.5	-11.6	-5.5	-5.0	32.5

Source: Ministry of Statistics and Programme Implementation

Growth in food products slows down sharply

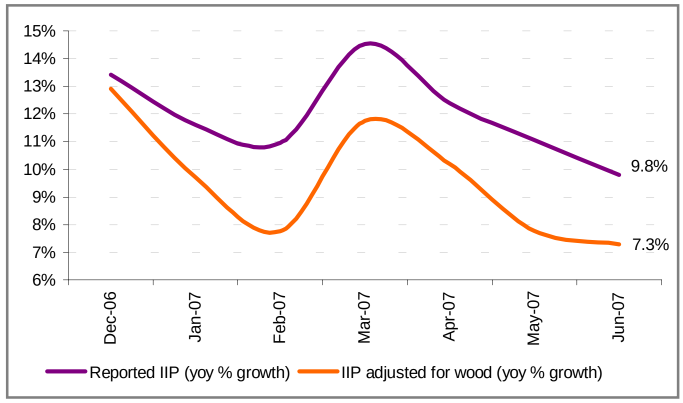
The sharp fall in food products growth to 1.3% is worth mentioning. We have been highlighting that such high double-digit growth in this sector as seen in the past few months (53.5% in April 2007 and 24.8% in May 2007) was unsustainable as the same was influenced by higher sugar production. However, the other sector that has been growing at high double digits (over 100%) is the wood products and it maintained its growth momentum at 103.9% in June 2007.

Adjusted for wood products IIP growth would moderate further

Our calculations suggest that the IIP numbers would moderate by 250 basis points to 7.3% if we replace the high growth in the wood products segment with the latter's average growth rate of 11% recorded in the months prior to the high growth rates that the segment started reporting December 2006 onwards.

The food products segment grew by 26.9% in July 2006. If the growth rate then was not influenced by seasonality and if we expect the current production trend in this sector to be maintained, then we could see a decline in production of food products in July 2007. This could lead to a fall in the manufacturing index and IIP on a month-on-month basis.

IIP adjusted for wood products



Source: Ministry of Statistics and Programme Implementation

Outlook

The IIP numbers have moderated with the key heavyweight sectors in the manufacturing segment showing signs of moderation. Capital goods production has remained robust, however growth in consumer durables has been weak mainly due to a slowdown in the demand for automobiles which has led many large players to cut production. Our view is that higher interest rates and lower export growth are leading to deceleration in industrial production. We expect the IIP numbers to moderate further going forward.

Telecommunication

Sector Update

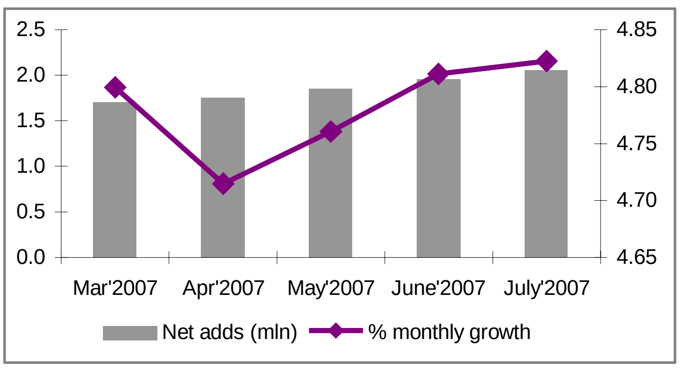
Record net adds

The GSM (global system for mobile communications) operators added 5.75 million subscribers in July 2007—that is higher than 5.38 million added in June 2007. This amounts to a growth of 4.2% (to 141.7 million subscribers) over the base of 136 million at the end of June 2007.

Bharti maintains its growth momentum

Bharti Airtel Ltd (BAL) reported record net adds of 2.06 million, taking its subscriber base to 44.8 million. BAL maintained a monthly growth of 4.7-4.8% over the last five months. But in absolute terms, the monthly net subscriber addition grew steadily from 1.7 million in March 2007 to 2.06 million in July 2007. We have factored in average net subscriber addition of 1.8 million per month (21.6 million in FY2008). The performance is slightly ahead of our expectations.

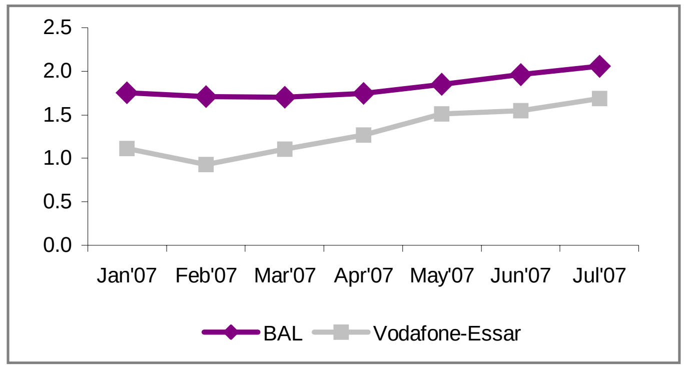
Steady increase in absolute net additions



Vodafone-Essar: Closing in the gap

Vodafone-Essar reported net subscriber addition of 1.7 million, which amounts to a growth of 5.3% over the base of 31.8 million in June 2007. The monthly growth is higher than that of BAL for the third consecutive quarter. In absolute terms also, the company is closing the gap with the market leader BAL.

Monthly net additions (in million)



Others

Other private operators such as Idea and Spice also maintained the growth momentum in July, with additions of 0.88 million and 0.37 million subscribers respectively. On the other hand, Bharat Sanchar Nigam lagged behind with 0.55 million adds during July 2007.

Monthly summary

GSM	Total subscriber base			Net additions		Share of net additions (%)	
	Jun-07	Jul-07	% change	Jun-07	Jul-07	Jun-07	Jul-07
BHARTI	42,703,938	44,763,391	4.8	1,960,213	2,059,453	36.4	35.80
HUTCH+BPL	31,839,509	33,531,653	5.3	1,547,760	1,692,144	28.7	29.40
BSNL	28,423,283	28,979,034	2.0	428,873	555,751	8.0	9.66
IDEA	16,126,396	17,004,327	5.4	859,778	877,931	16.0	15.26
MTNL	2,608,811	2,668,973	2.3	60,916	60,162	1.1	1.05
RELIANCE	4,347,593	4,347,593	0.0	0	0	0.0	0.00
Others	9,945,662	10,452,495	5.1	529,697	506,833	9.8	8.81
	135,995,192	141,747,466	4.2	5,387,237	5,752,274		

The author doesn't hold any investment in any of the companies mentioned in the article.

FMCG

Sector Update

Q1FY2008 earnings review

Companies from the fast moving consumer goods (FMCG) sector have reported an impressive performance for the first quarter of FY2008. On an average, the top line and bottom line of the FMCG industry grew by 17.5% and 20.6% respectively during the quarter. In spite of the rising pressure of high raw material prices, the industry was able to maintain its margins in Q1 and this was a positive surprise. The revenue growth was driven by higher volumes and improved pricing power. The strong growth in the revenues of companies like ITC (despite price hikes and declining volumes), Hindustan Unilever Ltd (HUL), Dabur India and Nestle indicates that the performance of the sector would be strong in the coming quarters.

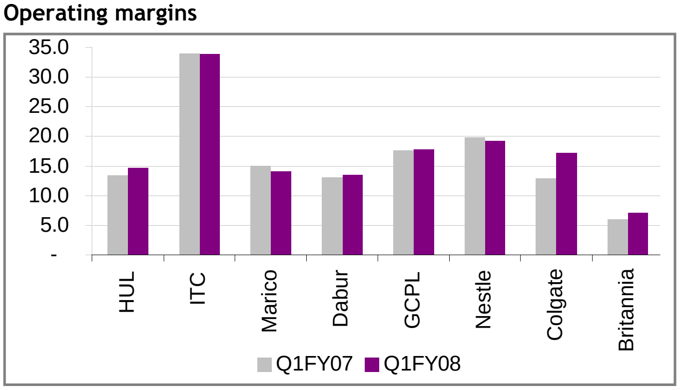
A double-digit revenue growth

The FMCG sector recorded a robust growth in the first quarter driven by increased spending in both rural and urban markets. Moreover, a shift from the unorganised sector to the organised sector in many categories such as biscuits, paints and detergents, and the roll-out of the retail formats also fueled growth. A strong growth in HUL's soaps and detergent segment (revenues up 14.6% year on year [yoy]) and ITC's cigarette segment (revenues up 8.9% yoy) came as a positive surprise. Companies like Marico, Dabur India, Godrej Consumer Products Ltd (GCPL) and Nestle have reported a revenue growth of +20% for the current quarter which is applaudable. We believe rising consumerism and improved pricing power would ensure a strong growth in the top line of the FMCG companies in the coming quarters.

Margins sustain despite rising costs

Despite rising raw material prices FMCG companies were able to maintain their margins by effecting price hikes and saving costs.

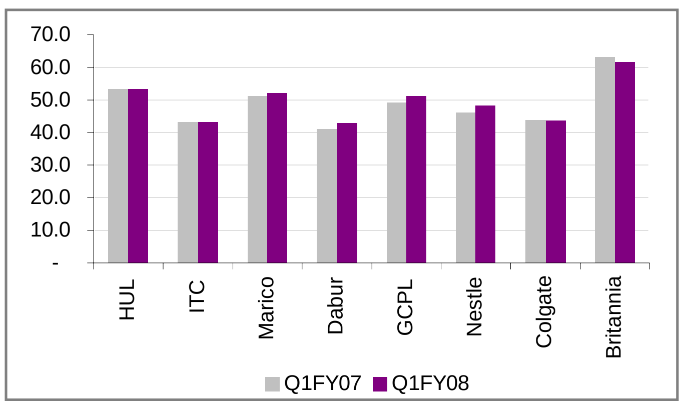
Operating margins



Pricing power returns...

The raw material cost as a percentage of sales was stable for companies like HUL and ITC. But companies like GCPL and Nestle witnessed some pressure on this front which was offset to some extent by raising product prices. This denotes the increased pricing power of these companies. For instance, Marico has been witnessing pricing pressure on edible oil in this quarter and has clearly indicated that any increase in its raw material cost would be passed on to the consumers. In fact, the company had increased the price of *Saffola* by 2-3% in the beginning of the year and the price hike had not affected the volumes of the brand at all. Britannia Industries and Colgate India also had a better quarter with their input costs stabilising, thereby leading to margin improvement. We believe better pricing power and improved product mix would help the industry to maintain its margins in the coming quarters.

Raw material cost as a % of sales

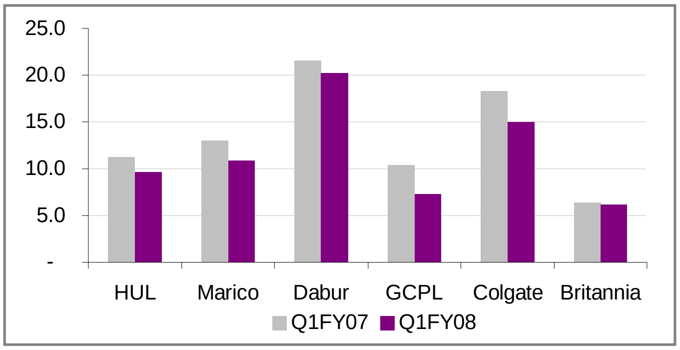


...lower ad spend helps

The industry spent less on advertising in this quarter in order to protect the margins in the wake of the rising costs. Moreover, the pace of product launches in this quarter was also slower. With the whole industry following the same practice, most of the players' share of voice target was also met.

The advertising spend as a percentage of net sales decreased by around 150-200 basis points for most of the companies. GCPL and Colgate India, however, reduced their advertising spend drastically (by 305 basis points and 332 basis points respectively) during the quarter. Such low advertising spends, we believe, are not sustainable in the long term in view of the new launches in the pipeline and the increasing competition. Britannia Industries maintained its advertising spend during the quarter in order to maintain its market share in a highly competitive market whereas ITC emerged as an aggressive player.

Advertising spend as a % of sales



Outlook and valuation

We believe with the rising consumerism, the roll-out of the retail formats and increasing penetration of the FMCG companies in the rural market, the growth momentum in the industry is expected to remain strong in the coming quarters. Moreover, better pricing power and improved product mix would help the industry to maintain its margins in the coming quarters.

Our preferred long-term picks in the FMCG sector are HUL, ITC and Marico. HUL has shown a strong revenue growth with a 30% increase in its earnings before interest, tax, depreciation and amortisation (excluding the losses from the water business) during the quarter, which is quite commendable.

ITC is another top pick which had been an underperformer for the past few months due to concerns over the implementation of the value added tax. But we had always insisted that the underperformance was a short-term aberration and one should look at the stock from a long-term perspective. The strong growth in the company's cigarette division in the first quarter in spite of declining volumes only reaffirms our faith in ITC.

In view of the increased contribution from its high-margin products, its strong product basket and the fact that its Kaya business has achieved operational efficiency, we continue to be bullish on Marico as well.

Colgate India has reported a 13.3% growth for the current quarter with a bottom line growth of 69%. The robust growth in the bottom line was due to lower advertising spend and staff costs as well as a lower tax rate. With the fiscal benefits from the company's new toothpaste plant in Baddi expected to continue till FY2012, the company is expected to record a strong growth in its bottom line in the coming quarters. We believe that the healthy revenue growth is also sustainable as a huge section of the rural market, where a large number of consumers have yet to move from powder to paste, is still untapped.

GCPL is trading at a lower valuation on a comparative basis but its decreasing market share in the hair colour segment and strategy to maintain its margins with focus on low-margin loose powder hair dye remain causes for concern. Nestle's valuations are already factoring in the robust growth recorded in the past few quarters. With the commencement of the manufacturing unit in a tax-efficient zone, the bottomline is expected to show a strong growth in the coming quarters, which could trigger an upward movement in the company's stock price.

Till now, the absence of aggressiveness in Dabur India was a cause for concern. However, the company's newfound appetite for making acquisitions and floating new ventures (health and beauty format) has dispelled that concern. We believe Dabur India could be a good bet in the long run.

Valuation table

	CMP		EPS		PE	
	(Rs)	FY07	FY08	FY09	FY08	FY09
HUL#	196.0	7.0	8.5	9.6	23.1	20.4
% yoy chg			*21.4*	*12.9*		
ITC	163.0	7.2	7.9	9.6	20.6	17.0
% yoy chg			*9.7*	*21.5*		
Marico	58.0	1.9	2.6	3.3	22.3	17.6
% yoy chg			*36.8*	*26.9*		
Dabur*	102.6	3.3	3.9	4.6	26.3	22.3
% yoy chg			*18.2*	*17.9*		
GCPL*	137.0	6.4	7.5	8.7	18.3	15.7
% yoy chg			*17.2*	*16.0*		
Nestle#*	1270.0	32.6	42.5	50.8	29.9	25.0
% yoy chg			*30.4*	*19.5*		
Colgate*	392.0	13.8	16.7	19.5	23.5	20.1
% yoy chg			*21.0*	*16.8*		
Britannia*	1609.0	45.0	74.8	94.3	21.5	17.1
% yoy chg			*66.1*	*26.1*		

*Consensus estimates, # December ending

The author doesn't hold any investment in any of the companies mentioned in the article.

Cement

Sector Update

Top three majors register a superlative dispatch growth

The top three cement majors registered a superlative dispatch growth in July. ACC's dispatches grew by 15.2% year on year (yoy) to 1.64MMT (million metric tonne) led by the higher capacities at its Lakheri and Kymore plants. Ambuja Cements recorded the highest dispatch growth of 19.5% yoy to 1.39MMT, whereas the AV Birla Group registered a dispatch growth of 13.1% yoy to 2.4MMT. We believe the growth looks inflated as most parts of India witnessed heavy monsoons in July last year. This is substantiated by the fact that the month-on-month decline in dispatches for July last year is very steep compared with that of the current year.

Particulars	July 2007	% yoy chg
ACC	16.40	15.2
Gujarat Ambuja	1.39	19.5
AV birla Group	2.399	13.1

Source: Company

Particulars	June 2006	July 2006	% mom chg
ACC	1.5	1.4	-7.6
Gujarat Ambuja	1.4	1.2	-15.6
AV birla Group	2.5	2.1	-14.3
	June 2007	July 2007	% mom chg
ACC	1.7	1.6	-5.7
Gujarat Ambuja	1.4	1.4	0.5
AV birla Group	2.5	2.4	-5.1

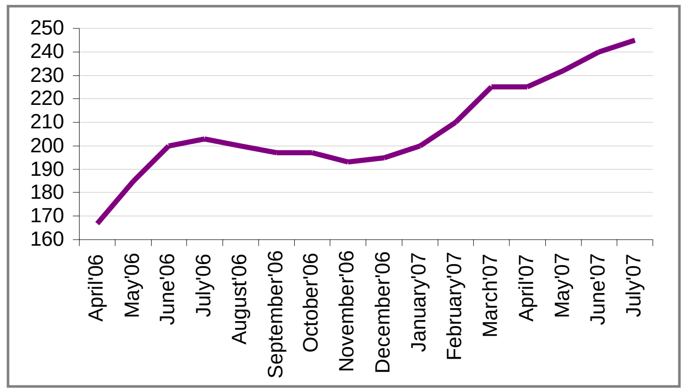
Source: Company, Sharekhan

Prices in the South on the upward trajectory

More than 100% capacity utilisation of cement companies based in South coupled with their slower capacity addition has made the cement prices sky rocket in the region. As mentioned in our earlier updates, the wholesale cement prices in Tamil Nadu increased by Rs6-7 per bag in May and again by Rs7-9 per bag in June, whereas prices in Andhra Pradesh increased by Rs5-9 per bag in the first week of June. This was visible in the realisation growth of both of the south India based companies India Cements and Madras Cements, which witnessed a quarter on quarter realisation growth of 10-11% respectively.

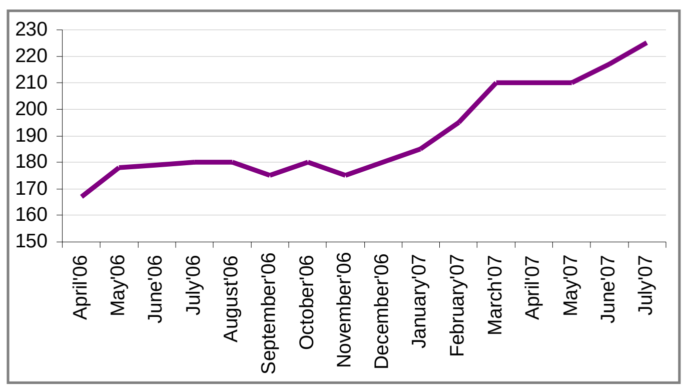
With the finance minister officially removing the price freeze, the cement manufacturers did not shun from hiking the cement prices in July as well. The cement prices increased by Rs5-10 per bag in Tamil Nadu and Andhra Pradesh in July, whereas the prices in Bangalore went through the roof. Cement prices in Bangalore increased by Rs15-20 per bag in June and are currently hovering in the range of Rs265-275 per bag. The dealers expect the prices to rise by another Rs5 per bag on August 15.

Prices in Chennai



Source:Sharekhan

Prices in Andhra Pradesh



Source:Sharekhan

Prices remain more or less same in the North and East

The cement prices in the North have maintained the status quo in the last couple of months. In Delhi prices increased by Rs3 per bag in July and currently stands at Rs225 per bag. Wholesale Prices in Jaipur remained constant at Rs198 per bag. Prices in Kolkatta increased by Rs2 per bag each in July and August and currently stand at Rs232 per bag. With rains round the corner, the dealers expect the prices to remain constant in the coming months.

Prices in the Western region broadly remain constant

Cement prices in Gujarat increased by Rs2 per bag in July after remaining stagnant for three months. The prices at present stand at Rs215-220 per bag. Prices in Mumbai have remained constant at Rs245-250 per bag in the last couple of months.

Cement earnings review

The cement earnings for most of the companies under our coverage were in line with our expectations. But the performance of the companies at the operating level was a mixed bag, though higher other income component for most of the companies cushioned the bottomline growth.

Overall dispatches for the companies under our coverage grew by 9.1% yoy with ACC and Shree Cements registering a higher growth of 14.5% and 25.4% yoy respectively.

With the average realisations growing by 15% yoy, the net sales grew by a robust 26.4% yoy. Our south based companies namely India Cements and Madras Cements registered a robust qoq realisation growth of 10% and 9% respectively, thanks to the increase in the prices in May and June.

As the expenditure growth at 24.5% yoy lagged the topline growth, the earnings before interest, tax, depreciation and amortisation (EBITDA) grew faster at 30.4% yoy. On the back of higher interest income on surplus cash, the net profit grew much faster by 45%.

Heavy rains in Gujarat...Ambuja Cements shuts plant

Due to the heavy rains in Gujarat in August, Ambuja Cements had to shut the operations at its Gujarat facility at Ambujanagar. The shutdown will impact the volumes for the company as Ambujanagar contributes more than 25% of the company's overall volumes.

Even Saurashtra Cements and Gujarat Sidhee Cements have stopped their operations temporarily. We believe that the monsoons being heavy in this month, broadly the dispatch growth for most companies (except those based in the south) will be slower because of lower volumes coupled with the higher base of last year.

Outlook

With the onset of monsoons in most parts of the country, the construction activity will take a backseat and so will the cement demand. As already visible, cement plants in Gujarat have had to shut operations on account of floods. Consequently, we expect cement prices in all parts of the country (except South) to maintain the status quo.

But we believe that Tamil Nadu and parts of Andhra Pradesh will continue to see higher demand in the near future and a consequent rise in cement prices as the monsoons arrive later in the region.

Result table for Sharekhan universe

		Net sales			EBITDA			Net profit	
Company	Q1FY08	Q1FY07	% yoy	Q1FY08	Q1FY07	% yoy	Q1FY08	Q1FY07	% yoy
ACC	1867.9	1462.0	27.8	544.4	455.0	19.6	351.4	259.1	35.6
Ultratech	1365.3	1180.3	15.7	433.5	374.6	15.7	259.4	210.8	23.0
India Cements	701.2	485.2	44.5	264.3	165.6	59.6	183.4	112.7	62.8
Madras Cements	469.3	340.9	37.7	182.7	136.4	33.9	100.5	78.9	27.4
Shree Cement	425.8	309.4	37.6	182.3	137.5	32.6	117.0	90.4	29.4
JK Cement	326.4	279.5	16.8	96.5	65.7	46.9	52.5	33.0	59.1
Orient Paper	293.1	258.4	13.4	77.7	53.4	45.5	44.6	26.0	71.5
Grasim	1390.0	1096.8	26.7	491.0	376.5	30.4	511.7	311.9	64.0
Jaiprakash	517.3	408.0	26.8	192.9	126.1	53.0	140.0	92.0	52.2
Overall	7356.2	5820.6	26.4	2465.3	1890.8	30.4	1760.5	1214.8	44.9

Source: Sharekhan

Per tonne analysis

	Volumes		Realisation		Cost		EBITDA	
Particulars	Q1FY08	% yoy	Q1FY08	% yoy	Q1FY08	% yoy	Q1FY08	% yoy
ACC	5.3	14.5	3524.3	11.6	2496.6	14.9	1027.7	4.5
Ultratech	4.5	0.4	3054.3	15.2	2084.4	15.1	969.9	15.2
India Cements	2.3	6.5	3048.6	22.8	1899.1	16.1	1149.5	35.6
Madras Cements	1.45	16.1	3236	18.6	1976.1	20.7	1259.9	15.4
Shree Cement	1.4	25.4	3019.9	9.7	1726.0	12.9	1293.9	5.8
JK Cement	0.9	-1.1	3564	25.2	2510.4	17.5	1053.6	48.6
Orient Paper	0.7	12.6	2621	7.0	1491.0	16.5	1130.0	-3.3
Grasim	4.0	10.6	3510.1	14.6	2270.2	12.9	1239.9	17.9
Jaiprakash	1.66	5.7	3116	19.9	1965	9.4	1151.0	43.3
Overall	22.1	9.1	3326.1	15.8	2211.4	14.1	1114.7	19.5

Source: Sharekhan

We believe that the removal of the price-freeze will augur well for the companies under our coverage and taking cognizance of that we have revised our earnings estimates for the same. We remain bullish on Grasim and Jaiprakash Associates as their non-cement businesses will sufficiently cushion the downturn in the cement cycle. The fact that India Cements will be a 14.5MMT company by FY2009 coupled with the bullish pricing scenario going ahead makes the company attractive at current levels. We also like Orient Paper as it trades at a cheap valuation of USD25 at its expanded capacity of 5MMT.

Valuation table

Company	Price	PER		EV/EBITDA		EV/Tonne	
	Target	FY08E	FY09E	FY08E	FY09E	FY08E	FY09E
ACC	1210	12.1	12.6	7.7	7.7	202.5	187.4
Ultratech	1100	11.0	9.6	6.5	5.5	169.8	135.5
Shree Cement	1625	10.1	9.3	5.8	4.8	133.9	98.6
JK Cement	200	5.7	6.6	4.1	5.0	87.9	66.3
Madras Cements	3700	9.0	7.4	5.4	4.6	134.6	114.6
India Cement	231	7.9	7.0	5.2	4.0	146.4	116.9
Orient Paper	680	4.6	4.6	2.7	3.1	53.0	47.0

The author doesn't hold any investment in any of the companies mentioned in the article.

Mutual Gains

Mutual Fund

Sharekhan's top equity fund picks

Record foreign fund inflows enabled the market to advance by an appreciable 6.1% in July. However, the upward march was bumpy with breathtaking climbs, stomach-churning drops et al. Not content with conquering the lofty levels of 15k, the market rapidly gained another 800 points in less than a fortnight to close at an all-time high of 15,869 on July 24. Just when expectations were building up that the market would comfortably cross even the magic figure of 16k before the month got over, it plummeted by over 541 points on July 27, in reaction to the weakness in global markets. Recovery was rapid but short-lived. Thus even though the market took another round of cash reserve ratio (CRR) hike in its stride and closed up 300 points on July 31, it plunged by a mind-numbing 620 points the very next day when the other global markets crashed on heightened US subprime lending concerns. Clearly, the market is choosing to take its cue from the West at the moment. Considering that there is much trouble brewing in the West, that is a cause for concern.

All eyes are on the USA, where the subprime mortgage crisis is unfolding itself. The sharp rise in defaults on subprime loan repayments and foreclosures on account of the rising interest rates in the USA has forced some of the biggest US subprime lenders to either shut shop or file for bankruptcy. There are fears that the crisis is spreading to the other mortgage segments also and might ultimately result in a severe credit crunch. A crunch in the housing market, in turn, could slow down consumer spending-consumer spending grew at a mere 1.3% in the second quarter vs 3.7% in the first quarter. Any downturn in the US economy could spell trouble for our market as it would not only affect our exports and hence our economy but also slow down the fund flows into our market. However, it will be some time before the extent of the damage caused by the bursting of the housing bubble becomes clear.

Fortunately, in spite of everything the broader American economy appears to be in good shape. The unemployment rate remained stable at 4.6% and 92k new jobs were added in July 2007. In the second quarter, the US GDP grew at the fastest pace in more than a year at 3.4% as against 0.6% in the first quarter of 2007. Inflation too remains within the comfort range of the US Federal Reserve (Fed). The problem has till now remained limited to the housing sector and not affected the rest of the economy. But if the crisis balloons this view could change.

Meanwhile, there is another frightening aspect of the subprime mortgage crisis. The recent meltdown in the equity markets across the world was triggered by reports of losses suffered by large funds with exposure to the US subprime lending market. For instance, two funds of Bear Sterns Cos., the fifth-largest US securities firm, collapsed last month while Australia's Macquarie Bank has voiced its fears that some of its funds may post losses. It is feared these foreign institutional investors (FIIs) may sell their profitable investments in the emerging markets to offset the losses suffered on account of the collapse of the US subprime lending market. That's not all, the yen has appreciated by a good 5.3% against the dollar in the past few weeks which is triggering large-scale unwinding of the carry trades financed with the Japanese currency.

Not all concerns that India Inc has to deal with are imported though. There are problems aplenty on the home turf as well. Firm interest rates and strong rupee continue to hurt our exports, which (minus petroleum products), as per our estimates in rupee terms, actually saw a decline of 1% in June this year vs a 37% growth in June 2006. The slowdown in the export sector may ultimately slow down the earnings growth of the domestic companies. That the strong rupee and high interest rates have already affected the earnings growth momentum was evident from the first quarter results of corporates. For the first time in several quarters, the earnings of the corporate sector failed to meet expectations when adjusted for the foreign exchange gains.

Thus the sky does appear to be overcast. But as always, there's a silver lining. India continues to grow at a faster pace than most other emerging economies and thus remains the toast of the FIIs. Just to give you an idea, the FIIs made net purchases worth over Rs17,000 crore in the first three weeks of July alone-that is almost equivalent to what they had invested in April, May and June put together. Of course, the global concerns that we just talked of might result in some mass withdrawals in the near term but the fact remains that the Indian economy's impressive performance would be able to sustain the foreign fund inflows in the medium term.

When all's said and done, there are concerns, both global and homegrown, that might keep the markets volatile in the near term. Hence caution is advised. Rather than rushing in on a correction, we would wait and watch how the global and domestic factors unfold. We prefer telecom and fast moving consumer goods sectors as well as select stocks from cement, engineering and capital goods sectors with lower valuations.

We have identified the best equity-oriented schemes available in the market today based on the following parameters: the past performance as indicated by the returns, the Sharpe ratio and Fama (net selectivity).

We have identified the best equity-oriented schemes available in the market today based on the following 3 parameters: the past performance as indicated by the one and two year returns, the Sharpe ratio and Fama (net selectivity).

The past performance is measured by the one and two year returns generated by the scheme. Sharpe indicates risk-adjusted returns, giving the returns earned in excess of the risk-free rate for each unit of the risk taken. The Sharpe ratio is also indicative of the consistency of the returns as it takes into account the volatility in the returns as measured by the standard deviation.

FAMA measures the returns generated through selectivity, ie the returns generated because of the fund manager's ability to pick the right stocks. A higher value of net selectivity is always preferred as it reflects the stock picking ability of the fund manager.

We have selected the top 10 schemes upon ranking on each of the above 4 parameters and then calculated the mean value of each of the 4 parameters for the top 10 schemes. Thereafter, we have calculated the percentage underperformance or over performance of each scheme (relative performance) in each of the 4 parameters vis a vis their respective mean values.

For our final selection of schemes, we have generated a total score for each scheme giving 30% weightage each to the relative performance as indicated by the one and two year returns, 30% weightage to the relative performance as indicated by the Sharpe ratio and the remaining 10% to the relative performance as indicated by the FAMA of the scheme.

All the returns stated below, for less than one year are absolute and for more than one year the returns are annualised.

We present below our recommendations in the equity-oriented mutual fund category.

Aggressive Funds

Mid-cap Category

Scheme Name	NAV	Returns as on Jul 31, 07(%)		
		3 Months	1 Year	2 Years
SBI Magnum Midcap	26.64	19.62	67.97	50.28
Reliance Growth	324.13	17.65	67.41	46.66
Birla Mid Cap	80.30	23.03	63.48	46.08
ICICI Prudential Emerging STAR	33.21	14.79	62.79	47.61
Sundaram BNP Paribas Select Midcap	102.13	12.67	39.50	48.77
Indices				
BSE Sensex	15550.99	12.10	44.74	42.57

Opportunities category

Scheme Name	NAV	Returns as on Jul 31, 07(%)		
		3 Months	1 Year	2 Years
ABN AMRO Opportunities	25.94	21.39	70.81	51.67
Fidelity Equity	25.14	15.18	61.52	44.96
DSP ML Opportunities	64.42	15.02	48.91	45.37
Franklin India Flexi Cap	24.07	14.79	47.06	44.48
Kotak Opportunities	33.78	14.36	50.46	42.29
Tata Equity Opportunities	68.75	15.91	54.00	42.63
Franklin India Opportunity	29.51	14.81	55.89	44.37
Indices				
BSE Sensex	15550.99	12.10	44.74	42.57

Equity diversified/conservative funds

Scheme Name	NAV	Returns as on Jul 31, 07(%)		
		3 Months	1 Year	2 Years
Birla SunLife Frontline Equity	60.21	14.64	57.21	47.04
DSP ML Top 100 Equity	67.33	12.81	53.17	48.18
SBI Magnum Multiplier Plus 93	63.38	17.07	57.00	51.59
HDFC Equity	172.33	14.00	48.98	45.68
Birla SunLife Equity	220.83	18.58	66.99	47.93
Franklin India Prima Plus	162.39	14.07	57.76	48.30
SBI Magnum Global Fund 94	47.75	10.99	55.23	50.23
SBI Magnum Equity	32.68	14.91	54.39	47.60
ABN AMRO Equity	32.46	19.65	62.06	46.80
HDFC Growth	58.72	20.86	57.86	46.62
Indices				
BSE Sensex	15550.99	12.10	44.74	42.57

Thematic/Emerging trend funds

Scheme Name	NAV	Returns as on Jul 31, 07(%)		
		3 Months	1 Year	2 Years
DSP ML India Tiger	40.33	18.20	69.26	56.82
Tata Infrastructure	29.26	22.97	66.66	55.97
SBI Magnum Sector Umbrella - Contra	44.29	13.97	54.00	49.13
SBI Magnum Sector Umbrella Emerging Businesses	34.41	17.84	57.77	32.94
Templeton India Growth	77.40	12.99	47.79	37.63
Indices				
BSE Sensex	15550.99	12.10	44.74	42.57

Balanced funds

Scheme Name	NAV	Returns as on Jul 31, 07(%)		
		3 Months	1 Year	2 Years
Birla SunLife 95	208.64	14.47	48.82	33.35
HDFC Prudence	130.20	12.79	44.65	36.13
FT India Balanced	37.70	12.16	41.66	33.16
Tata Balanced	57.54	11.33	44.40	33.94
DSP ML Balanced	44.01	12.10	39.59	34.01
SBI Magnum Balanced	39.35	9.85	37.20	33.33
Indices				
Crisil Balanced Fund Index	2697.03	8.25	28.64	25.58

Tax planning funds

Scheme Name	NAV	Returns as on Jul 31, 07(%)		
		3 Months	1 Year	2 Years
PRINCIPAL Tax Savings	94.24	20.47	69.77	49.78
Birla SunLife Tax Relief 96	112.51	21.42	65.63	45.41
Sundaram BNP Paribas Taxsaver	30.61	11.15	48.63	39.25
Indices				
BSE Sensex	15550.99	12.10	44.74	42.57

Risk-return analysis

The charts on the following pages give you a snapshot of how the mutual funds have performed on the risk-return parameters in the past. We have used the bubble analysis method to measure their performances on three parameters viz risk, return and fund size. The risk is measured by standard deviation, which measures the average deviation of the returns generated by a scheme from its mean returns. We have tried to explain the same with the help of a diagram, which is divided into four quadrants, with each quadrant containing funds of a particular risk-return profile. The size of the bubble indicates the size of the fund.

The funds in the **high-risk high returns** quadrant follow a very aggressive approach and deliver high absolute returns compared to its peers albeit at a higher risk.

The funds in the **low-risk high returns** quadrant outperform the peer group on the risk-adjusted returns basis as they deliver higher returns compared to its peers without exposing the portfolio to very high risk.

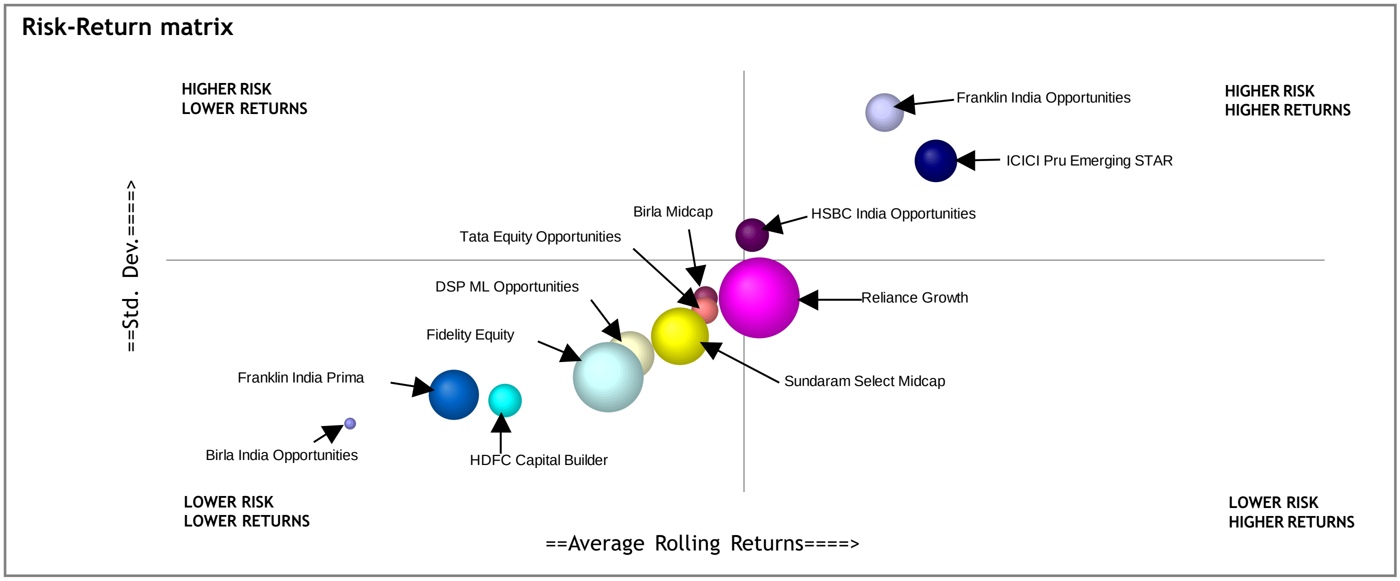
The funds in the **low-risk low returns** quadrant are not very aggressive and provide lower absolute returns, taking lower risks.

The funds in the **high-risk low returns** quadrant underperform the peers on the risk adjusted returns basis as they adopt a high-risk strategy but the returns fail to compensate the risk taken by the fund.

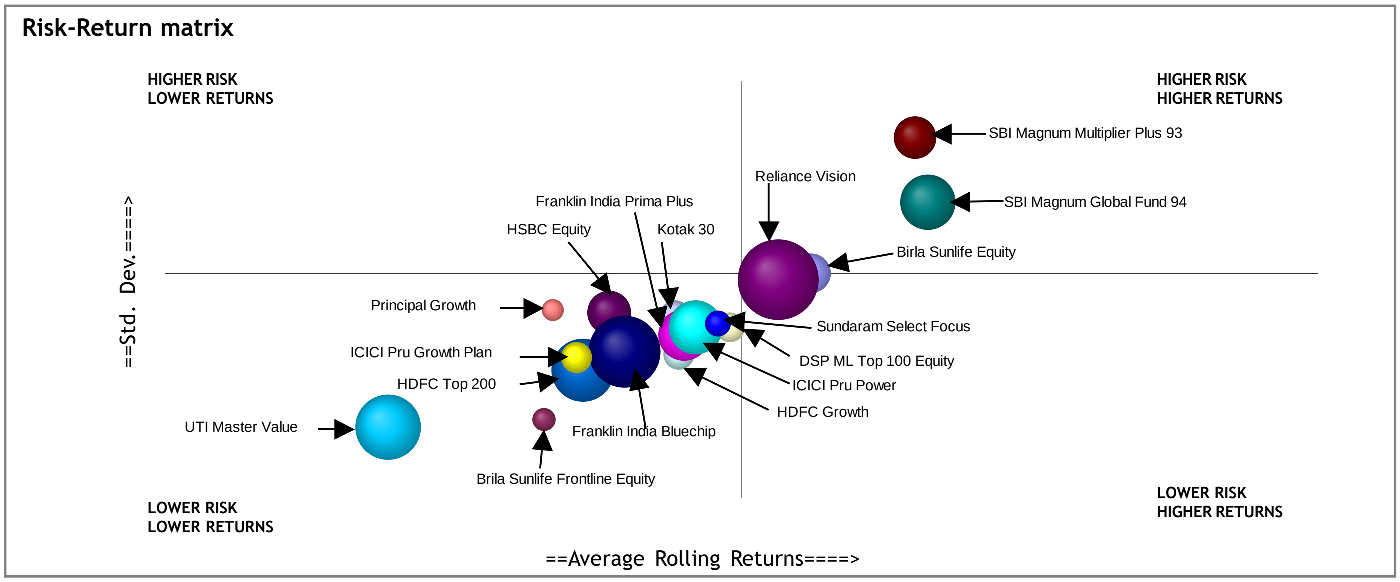
For aggressive, conservative and tax planning funds, risk is measured in terms of two years' volatility while returns are measured as two years' average rolling returns as on July 31, 2007. For thematic and balanced funds, risk is measured in terms of one year's volatility while returns are measured as one year's average rolling returns as on July 31, 2007.

Every individual has a different investment requirement, which depends on his financial goals and risk-taking capacities. We at Sharekhan first understand the individual's investment objectives and risk-taking capacity, and then recommend a suitable portfolio. So, we suggest that you get in touch with our Mutual Fund Advisor before investing in the best funds.

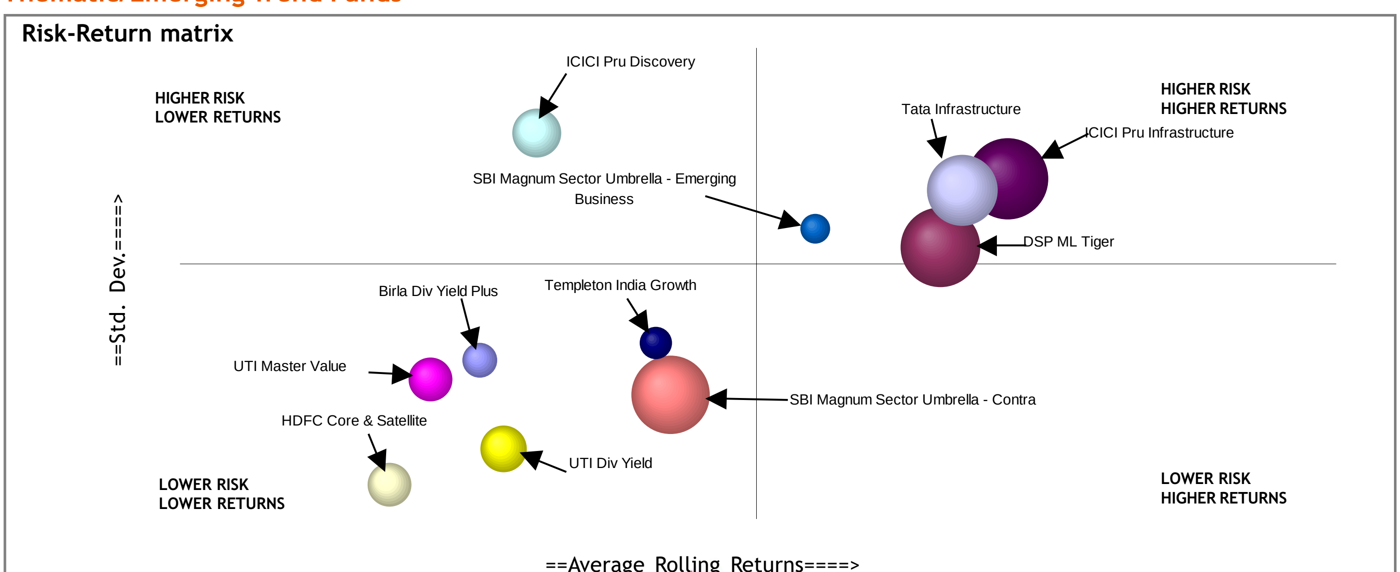
Aggressive Funds



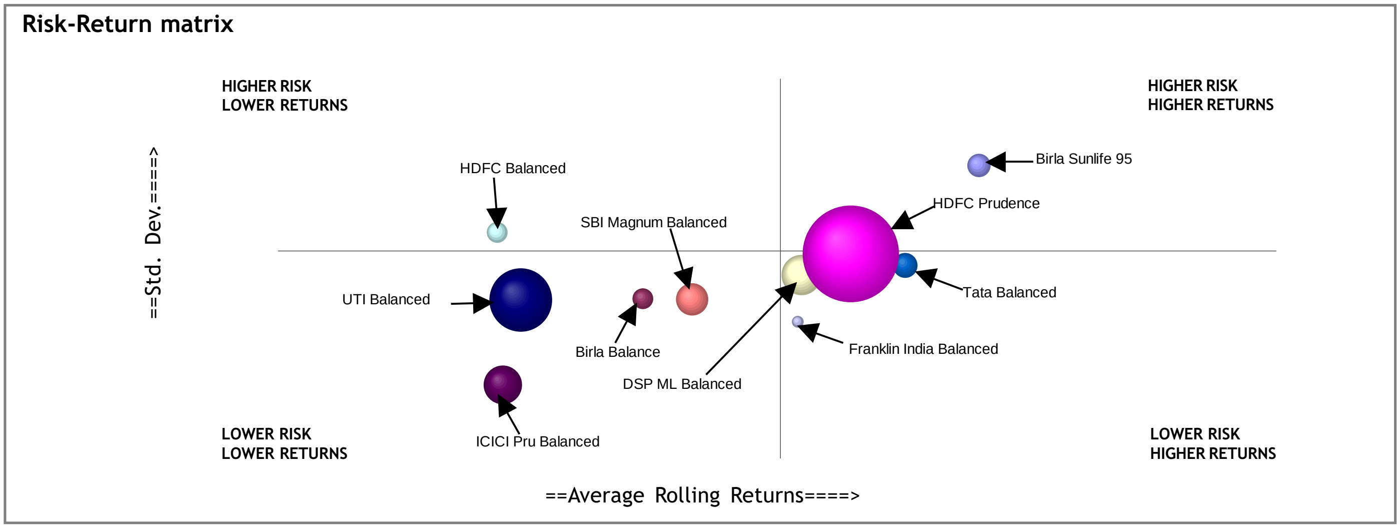
Equity Diversified/Conservative Funds



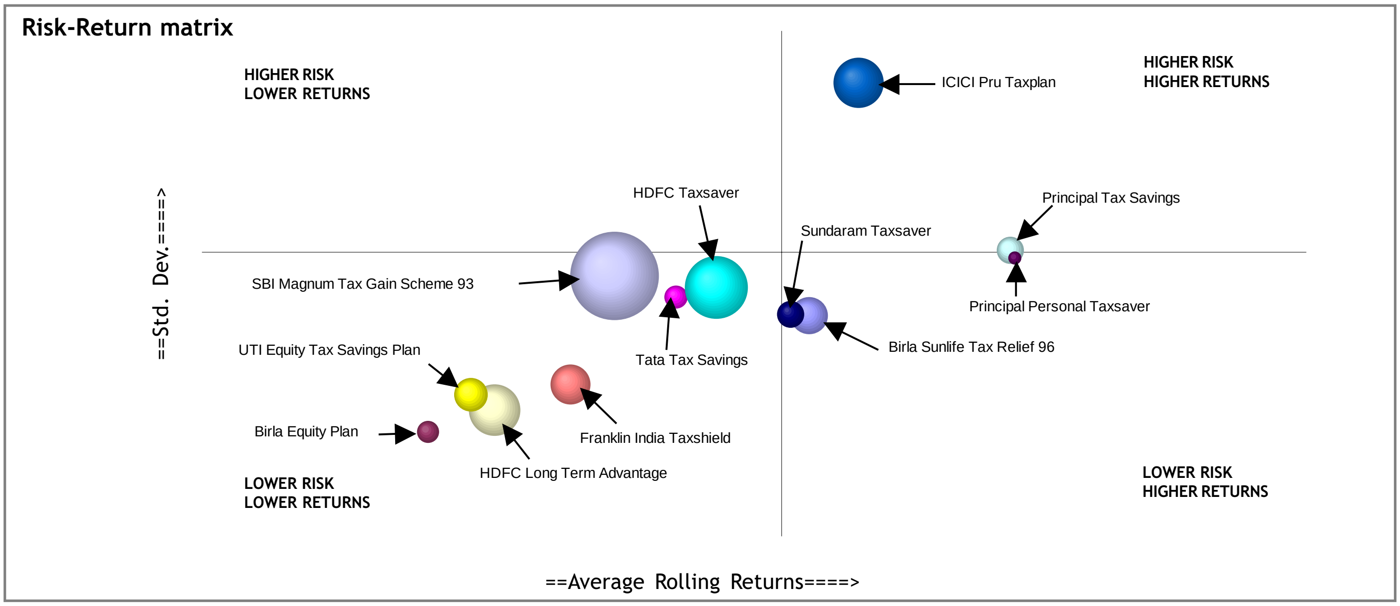
Thematic/Emerging Trend Funds



Balanced Funds



Tax Planning Funds



Sharekhan Stock Ideas

Evergreen

HDFC Bank
Infosys Technologies
Reliance Industries
Tata Consultancy Services

Apple Green

Aditya Birla Nuvo
ACC
Apollo Tyres
Bajaj Auto
Bank of Baroda
Bank of India
Bharat Bijlee
Bharat Electronics
Bharat Heavy Electricals
Bharti Airtel
Canara Bank
Corporation Bank
Crompton Greaves
Elder Pharmaceuticals
Grasim Industries
HCL Technologies
Hindustan Unilever
ICICI Bank
Indian Hotels Company
ITC
Mahindra & Mahindra
Marico
Maruti Udyog
Lupin
Nicholas Piramal India
Ranbaxy Laboratories
Satyam Computer Services
SKF India
State Bank of India
Sundaram Clayton
Tata Motors
Tata Tea
Unichem Laboratories
Wipro

Cannonball

Allahabad Bank
Andhra Bank
Gateway Distriparks
International Combustion (India)
JK Cement
Madras Cement
Shree Cement
Tourism Finance Corporation of India
Transport Corporation of India

Emerging Star

3i Infotech
Aban Offshore
Alphageo India
Axis Bank (UTI Bank)
Balaji Telefilms
Cadila Healthcare
Federal-Mogul Goetze (India)
KSB Pumps
Marksans Pharma
Navneet Publications (India)
Network 18 Fincap
Nucleus Software Exports
Orchid Chemicals & Pharmaceuticals
ORG Informatics
Tata Elxsi
Television Eighteen India
Thermax

Ugly Duckling

Ahmednagar Forgings
Ashok Leyland
Aurobindo Pharma
BASF India
Ceat
Deepak Fertilisers & Petrochemicals Corporation
Genus Power Infrastructures
Hexaware Technologies
ICI India
India Cements
Indo Tech Transformers
Jaiprakash Associates
JM Financial
KEI Industries
NIIT Technologies
Punjab National Bank
Ratnamani Metals and Tubes
Sanghvi Movers
Saregama India
Selan Exploration Technology
South East Asia Marine Engineering & Construction
Subros
Sun Pharmaceutical Industries
Surya Pharmaceuticals
UltraTech Cement
Union Bank of India
Universal Cables
Wockhardt
Zensar Technologies

Vulture's Pick

Esab India
Orient Paper and Industries
WS Industries India